

## Conference Paper

# Protection of Foreign Investors in Foreign Investment Activities and its Implications to the Country

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**Abstract.**

In the interest of increasing national and economic development, Indonesia needs various kinds of support from all aspects. One of them is the presence of foreign investors. However, Indonesia is considered to not fully support the presence of foreign investors, so there are many investment constraints that have not been addressed comprehensively. To fulfill these interests, the Indonesian government formulated policies regarding investment and legal protection provided to foreign investors through Law Number 25 of 2007 concerning Investment. This study aims to determine legal protection and the implications of foreign investment activities in Indonesia. This study uses a normative juridical approach. The primary source of legal material is Law Number 25 of 2007 concerning investment. The source of secondary legal materials uses relevant literature. Data collection were done using the library study method. Data analysis were done using deductive analysis techniques. The data presentation technique uses a qualitative descriptive technique. The results of the study stated that legal protection for foreign investment (PMA) in Indonesia according to Law Number 25 of 2007 concerning investment is the application of the principle of equality for foreign and foreign investors. Legal protection is also given for actions of nationalization, acquisition of ownership, transfer of assets, transfers, and repatriation. Foreign investment has an important role in Indonesia to increase economic growth and increase national development.

**Keywords:** legal protection, investment, foreign, implication

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## 1. INTRODUCTION

Economic progress and national development in Indonesia must of course be supported by capital. Without a capital system, economic development becomes impossible. So far, the source of funds for national and economic development in Indonesia has come from within the country. However, funds originating from within the country are certainly not sufficient to maximize national and economic development in Indonesia. Therefore, the Indonesian government opens opportunities for foreign investors who wish to invest in Indonesia. Foreign investment has an important role in national development and the

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economy of a country, especially in a developing country. This is caused by foreign investment not only transferring goods capital, but also transferring knowledge sources and human capital capital [1]

Foreign investors in investment activities in Indonesia are certainly not free from the risk of disputes with the Indonesian government. The disputes that occur can be caused by various things, such as the revocation of business licenses for foreign investment by the Indonesian government, default or breach of contracts by foreign investors against the Indonesian government or vice versa, takeover or nationalization of foreign companies, or violations of investors' rights. which has been regulated in the law. Investment activities or foreign investment will not be separated from the existence of risks or problems. The risks or problems faced by foreign investors can be caused by factors of socio-economic and political conditions in a country. For example, a country in a state of economic crisis has caused some foreign investment to be invested and carried out in that country to be hampered or delayed [2].

Legislative conditions, social, economic, political, also affect the interest of prospective investors before deciding to invest their capital. According to Muchtar Kusumaatmadja, existing statutory provisions in a country also affect the considerations of potential foreign investors. The existence of inconsistencies in investment regulations in a country can become a confusion and affect his decision to invest in Indonesia.

According to Aminuddin Ilmar in Wicaksono (2021), foreign investment in Indonesia can have positive impacts or benefits including; 1) alternative solutions to increase economic development in Indonesia; 2) efforts to develop facilities and infrastructure for the development of the surrounding industry; 3) provide wider employment opportunities for host countries; 4) efforts to improve workers' skills and expertise through collaboration on industrial technology advances; 5) increasing the State's foreign exchange; 6) increase efficiency in the application of high production scale (*economics of scale*); 7) increase production for export needs so as to increase the country's foreign exchange.

To be able to overcome these conditions, the government formulated policies related to legal protection for investors. Efforts to formulate a legal protection policy aim to provide guarantees for foreign investors who want to invest in Indonesia and create a conducive flow of foreign investment, as well as stimulate the interest of foreign investors to invest in Indonesia. It is undeniable that Indonesia as a developing country needs the role of foreign investors to improve the economy in Indonesia, because foreign investment makes a sizeable contribution to the Indonesian government.

Based on this description, the question arises as to how the Indonesian government regulates legal protection for foreign investors in Indonesia? So this study aims to

determine the form of legal protection provided by the Indonesian government to foreign investors.

## 2. METHODOLOGY/ MATERIALS

This research was conducted using a juridical-normative approach. Normative juridical research is an activity to examine legal aspects to resolve a problem or risk that occurs based on positive law. Normative juridical research uses legal references and applicable laws and regulations [3].

The primary legal source used in the research is Law Number 25 of 2007 concerning Investment. Secondary legal sources used to support research and analysis use literature in the form of books, journals, scientific articles, and other relevant sources. Data collection used in normative juridical law research is carried out using library study techniques[4]. Data collection is carried out by collecting or conducting searches of regulations and other literature related to the main research issues (*library research*).[5]

The analytical method used in this study uses deductive research techniques. In reaching a conclusion, the researcher first uses deductive logical thinking, namely by placing legal norms, jurisprudence, or doctrine as the major premise. While the minor premise is in the form of supporting literature as a complement or analytical knife to get research conclusions. Meanwhile, the presentation of the research results uses a descriptive method, by describing the results of the research and the conclusions of the research.[6]

## 3. RESULTS AND DISCUSSIONS

### 3.1. Legal Protection against Foreign Investment

The laws governing foreign investment in Indonesia are listed in Law Number 25 of 2007 concerning Investment. Investment is an investment activity to carry out business activities in the territory of the Republic of Indonesia by foreign parties. Such foreign investment can be in the form of fully foreign-owned investment or cooperation in the form of joint ventures with the Indonesian government. Foreign investment can also be made with domestic parties, provided that foreign parties can invest a maximum of 95% of capital and domestic investors can invest a minimum of 5% of capital.[7]

Article 1 point 8 of the Investment Law states that what is meant by foreign capital is:

“Foreign Capital is capital owned by foreign parties or foreign countries, individuals from foreign countries, foreign business entities, foreign legal entities, and/or Indonesian legal entities which partially or wholly obtain/own capital by foreign parties.” So it can be concluded that foreign capital owners consist of the following: a. foreign countries; b. Individual citizens from foreign countries; c. Foreign enterprise; d. Foreign legal entity; e. Indonesian legal entities whose capital is wholly or partly owned by foreign parties.[8]

The investment or investment can be categorized into two types, including: a. Full investment of foreign capital; and b. Partly foreign investment by means of joint ventures with domestic investors.

According to Article 5 paragraph (2) of Law Number 25 of 2007 concerning Investment, it states that foreign investment must be made in the form of a limited liability company. Foreign investment must be carried out based on Indonesian law. Foreign investment must be made in the territory domiciled in the Republic of Indonesia.[9]

According to the Investment Law, the objectives of holding investment opportunities in Indonesia [10] include the following:

a. Increasing national economic growth in Indonesia; b. Expansion of new jobs; c. Increasing sustainable national economic development; d. Increasing the ability of business competitiveness at the national level; e. Capacity building and industrial technology in Indonesia; f. Increasing the development of the people’s national economy; g. Development and processing of potential economic power into real economic power through the use of funds/capital originating from within or outside the country; h. Improvement of community welfare.

Laws are created in society with the aim of being able to integrate and coordinate the interests of society which have the potential to conflict with one another. Protection means protecting something to avoid danger, these things are conflicts of interest or problems with goods. According to Satjipto Rahardjo, protection is providing protection for human rights in a situation where you are experiencing a loss or risk or problem caused by someone else negligence or intentional actions. This protection is given to each individual so that each individual can enjoy this form of legal protection or guarantee.[11]

Legal protection can be divided into two, namely preventive legal protection and repressive legal protection. Preventive legal protection is a form of legal protection with preventive measures. Preventive legal protection is really needed by the government and has an important role in situations of freedom of action, but the government still takes careful action on these steps before making decisions so as to avoid harmful risks from these policies. Meanwhile, repressive legal protection is legal protection

given after a dispute or risk or danger arises. Repressive legal protection can be carried out in various ways, such as through a dispute settlement institution (arbitration), mediation, and can be pursued through legal channels through the local court which has the authority to resolve the dispute. The legal protection provided can be in the form of sanctions, fines, imprisonment and additional penalties in accordance with the provisions of the Court.[12]

Business fields open to investment are business sectors that are permitted to invest, both for domestic investment and foreign investment. Usually, in investing, especially foreign investment, there are several business fields that are not allowed to invest at all and there are also business fields that are required to carry out cooperation between foreign capital and domestic capital.

Prior to the enactment of Law Number 25 of 2007 concerning Investment, policies regarding foreign investment in Indonesia were regulated in Law Number 1 of 1967 concerning Domestic Investment. Law Number 25 of 2007 strengthens investment laws in Indonesia and there is no longer any legal dualism in terms of investment in Indonesia, both by foreign and domestic parties.

Law Number 25 of 2007 concerning Investment in Chapter 3 and Chapter 4 regulates the reference and framework for the development of investment in Indonesia, both by foreign and domestic parties. The government through Policy Law Number 25 of 2007 aims to accelerate investment growth and create a conducive national business climate for the investment system in order to further enhance economic competitiveness. Of course the government's basic policy must consider fairness or equal treatment for domestic and foreign investors. The government seeks to provide guarantees and legal protection to every investor, starting with investment licensing and continuing through the investment process until the end of the investment agreement.[13]

Legitimate certainty is a variable that is closely related to the issue of guarantees provided by public authorities on the cash flows of recipient countries to unknown funders so that these funders no longer feel a bit hesitant before building their capital in Indonesia. Law Number 25 of 2007 concerning Investment provides legal certainty to all investors, both domestic and foreign regarding sanctions and equal treatment. In addition, the law contains provisions regarding nationalization and pricing as well as arrangements regarding the acquisition, transfer and repatriation of assets in foreign currency.

The Business Regulations state that public authorities must apply fair treatment to foreign and local financial backers. This is in accordance with the Investment Law Article 4 paragraph 2 letter (a). The next letter, letter (b), states that the government must

guarantee legal, business, and investor safety during the licensing process and after the capital hiding activity is stopped. Equal treatment of all financial backers is then underlined in Article 6 which states that in the practice of capital speculation, public authorities should have the option of implementing similar arrangements for unknown financial backers, regardless of which country the unknown financial backers come from. Investors who have previously made or made special agreements with the government are exempt from this provision. Examples include customs agreements, free trade zones, common markets, monetary unions, similar institutions, and bilateral, regional or other agreements between the Indonesian government and other governments.

The Government of Indonesia and foreign governments that are bilateral, regional or multilateral in nature related to certain privileges in the implementation of investment.[14] Article 6 UUPM is a form of realization of the principle of treatment applied by the Indonesian government to investors in Indonesia, both foreign investors and domestic investors. Article 6 UUPM is the answer to people's assumptions that the Indonesian government gives different treatment to domestic investors and foreign investors, such as provisions relating *totax holiday* and looser investment regulations than domestic investors.[15] The policy in Article 6 regarding the principle of fair treatment of all investors, especially in Article 6 paragraph (2) relates to bilateral international investment agreements between the Government of Indonesia and foreign governments. The agreement between the Indonesian government and the foreign government is made in the form of an Investment Guarantee Agreement (*Investment Guarantee of Agreement*).

Meanwhile, if there is an act of nationalization, it is explained in the next Article (Article 7), that the Indonesian government will not take over the ownership rights of investors, except in accordance with statutory regulations. The Indonesian government will of course provide compensation to these investors if there is an act of expropriation of ownership rights or nationalization. Compensation is determined and adjusted according to market prices. If the two of them do not reach an agreement regarding compensation or compensation, then the settlement can be carried out through an arbitration process. This provision can also be seen in Article 32 concerning government policies in implementing arbitration steps to reach a consensus in the event of a dispute.[16]

- a. If there are problems or disputes between the Indonesian government and investors, both parties should first take the path of deliberation to reach a consensus;
- b. If an agreement or consensus is not reached in the deliberation process, then the settlement of the dispute can be carried out by arbitration or alternative dispute resolution in accordance with statutory provisions;

c. If the dispute occurs between the Indonesian government and domestic investors, then the parties can take arbitration to resolve the dispute. If the arbitration steps taken do not result in an agreement, then the parties can take the court route;

d. If a dispute occurs between the Indonesian government and a foreign investor, then the parties to the dispute can take international arbitration to obtain an agreement.

Regulations regarding the issue of nationalization in Indonesia are now also being tightened. So that if the government wants to nationalize a company, it must be able to meet the applicable requirements according to the law. This form of policy is a form of the goodwill of the Indonesian government towards foreign investors to establish and create conditions for good cooperation between Indonesia and investors from other countries. Arbitration between the government and foreign investors can also be taken if during the investment process, the foreign investors and the Indonesian government do not find an agreement in terms of submitting the determination of the amount, type and method of payment of compensation. The act of nationalization is also a form of action or policy that is legally recognized internationally. However, with due observance of the applicable laws and regulations. A country that wants to take action to nationalize investment contracts, then this action must also be legalized and recognized internationally.[17]

In Articles 8 and 9, UUPM regulates the transfer of assets and transfer rights and repatriation in foreign currency. If the investor wishes to transfer assets, then the process is regulated in such a way by law. The transfer in question is the transfer of profits in the original currency of the capital on the basis of the exchange rate to the country of origin. Meanwhile, repatriation is the investor's right to regain their rights from the country of domicile to their nationality of origin.

Legal protection is also given to multilateral investment agreements. Although the Indonesian government has developed an investment policy and legal protection for bilateral investment agreements, this has been pursued with the aim that any risks and problems that may arise in the future can be handled by the Indonesian government. The risks that arise and have the potential to cause problems such as monetary transfers, breaches of contracts, nationalization actions, and risks arising from war or disturbance of state stability.

Another Indonesian government action was to ratify the Conventional Establishing the Multilateral Investment Guarantee (MIGA) convention, based on Presidential Decree No. 1 of 1986. This gave a positive view of Indonesia by foreign investors, because by doing so Indonesia had provided a guarantee of protection law for foreign investors on the risk of foreign investment in Indonesia. In addition, with the issuance of Law no. 25

of 2007 has provided a guarantee of legal protection and certainty for investors against the takeover of foreign companies as stated in Article 7 UUPM.

Law Number 25 of 2007 concerning Investment in Chapter 3 and Chapter 4 regulates the reference and framework for the development of investment in Indonesia, both by foreign and domestic parties. The government through the policy in Law Number 25 of 2007 aims to create a conducive national business climate for the investment system so that it further enhances the competitiveness of the national economy, and aims to accelerate the increase in investment. The basic policies set by the government must of course be able to consider fairness or equal treatment between foreign investors and domestic investors. The government is trying to create guarantees and legal protection for every investor, starting from the initial stage in the form of investment permits, the investment process, until the investment agreement has ended.

### **3.2. Implications of Legal Protection for Foreign Investors for the State**

So far, Indonesia is one of the countries that has not fully supported the presence of foreign investors. This is due to the many investment constraints faced by investors before deciding to invest in Indonesia. The main obstacle faced by foreign investors is the aspect of legal certainty. Therefore, this government through Law Number 25 of 2007 concerning Investment seeks to provide legal protection for every investor, both for foreign investors and domestic investors. Investment provisions are also based on international law. Indonesia also seeks through participation in the MIGA Convention (*Multilateral Investment Guarantee Agency*) to stimulate increased foreign investment.

Foreign investors certainly have an important role in improving the economy and national development in Indonesia. For example, if the country is facing a sluggish export, then investment is one of the efforts to supply the country's foreign exchange. Foreign investment plays a role in procuring capital in the form of funds to finance various kinds of development projects. So, it can be concluded that foreign investment has a positive effect on improvement and economic growth in Indonesia. Through foreign investment, there is also a transfer of knowledge and technology, where Indonesia can apply industrial or development technology from the investor's home country. Foreign investors also benefit from the transfer of knowledge and technology, namely increasing state income or foreign exchange in the country of origin of foreign investors (Harjono, Dhaniswara, 2016)



The world is now in the era of free trade under the auspices of the WTO. Investors need certainty and guarantees as well as legal protection before deciding to invest in a country. Rapidly developing international trade also creates competitive competition. Therefore, legal protection is one of the supporting aspects of increasing foreign investment activities in Indonesia. Apart from playing a role in the world of international and national trade, in fact foreign investment also has an impact on the development of business or trade at the small and medium business level. Free trade which is now developing opens opportunities for SMEs to have access to international markets, so that they can participate in exports. So, it can be concluded that foreign investment influences economic development from various aspects.

#### 4. CONCLUSION AND RECOMMENDATION

In order to create order and legal certainty for foreign investors who invest in Indonesia, the Indonesian government provides protection in Law Number 25 of 2007 concerning Investment. The legal protection provided by the Indonesian government to foreign investors according to the law is if in the future there are problems or risks faced by investors, including non-commercial risks. These provisions are listed in Article 6 to Article 9 UUPM. The legal protection provided by the Indonesian government is based on the principle of equal treatment of foreign and domestic investors. Legal protection is also given against nationalization actions, expropriation actions, asset transfers, transfers and repatriations. Legal protection is based on national law that applies in Indonesia, international law, and law that applies under the MIGA Convention.

The legal protection policies implemented in Indonesia certainly have influences or implications for foreign investment activities in Indonesia. Legal protection, guarantees and legal certainty for foreign investors in Indonesia affect the decisions of foreign investors to invest in Indonesia. Foreign investment has a very important role in national and economic development in Indonesia. Foreign investment plays a role in providing funds or capital, increasing industrial or economic technological progress, creating new jobs, increasing the potential of Small and Medium Enterprises to gain access to foreign production exports and increasing the country's foreign exchange reserves. However, to support this, the government must be able to issue appropriate and proportional policies. This will enable further foreign investment assistance activities to run efficiently and profitably in accordance with the objectives of Indonesian national law and development goals.

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